

FSOC 2017 Annual Report—A Subtle Shift in Tone that Signals the Possibility of Meaningful Change

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There are distinct, but subtle, shifts in tone in the FSOC's [2017 Annual Report](#), especially when compared to previous annual reports and read together with three recent Treasury reports on financial regulatory reform, each of which touches on the role of the FSOC.[1] Taken as a whole, the 2017 Annual Report and the other writings from the Treasury may be an advance signal for how the Mnuchin Treasury Department and the Chairs of each of the key financial regulatory agencies, all but one of whom will be Trump appointees by mid-2018, will work together on FSOC to further the financial regulatory reform goals of the Trump Administration. Notably, the 2017 Annual Report maintains the Mnuchin Treasury's position that the FSOC should play a central role, as opposed to the view of House Republicans who would emasculate the FSOC. We suggest that the following trends are worth watching.

Enhanced FSOC Coordination Role. Watch for the FSOC to take a more active coordination role in financial regulatory reform. The Treasury Bank and Credit Union Report recommends that the FSOC be given more power by Congress to appoint a lead agency for regulation and enforcement. Even in the absence of Congressional action, we believe that the FSOC, with the agreement of the Chairs of each of the financial regulatory agencies, could informally coordinate regulatory reform in a more active way than has been done in the past. The Treasury FSOC Report's focus on the FSOC's authority to recommend to member agencies actions to address identified risks may be a signal that the FSOC intends to use or threaten to use its power to encourage cooperation by recalcitrant independent agencies.

Jobs and Growth. As has been widely reported in the media, for the first time since the FSOC annual report was mandated by the Dodd-Frank Act, the 2017 Annual Report takes into account economic growth and jobs, a clear reference to the [Presidential Executive Order](#) and economic policy agenda. It is a significant signal for financial regulatory reform that the FSOC takes the view that economic growth can be achieved not only by preventing financial crises and their negative externalities but also by minimizing the unintended consequences of regulatory and compliance burdens.

Focus on Regulatory Burdens, Overlap and Tailoring. For the first time in the history of its annual reports, the FSOC has identified the risks of increased compliance costs and regulatory burdens for financial institutions as a potential threat to financial stability. The 2017 Annual Report makes it clear that member agencies should "where possible and without reducing the resilience of the financial system, continue to address regulatory overlap and duplication, modernize outdated regulations, and, where authority exists, tailor regulations based on the size and complexity of financial institutions." [2] The tonal shift in this direction to member agencies is striking. We are far away from the Obama FSOC, which argued in court that it was not required to take costs into account when designating a company as systemically important.

Greater Focus on Activities Rather Than Designations. The 2017 Annual Report, like other recent reports, urges a pivot from designations to activities-based regulation. This shift has been widely previewed in the Treasury FSOC Report and in the Treasury Asset Management and Insurance Report. Like the Treasury FSOC Report, the 2017 Annual Report defends the FSOC designation authority, although it is clear in context that this FSOC sees it as a tool to be used rarely. See our earlier [blog post](#) on the Treasury FSOC Report published on November 20, 2017.

Other Topics. The 2017 Annual Report calls out a number of specific areas for regulatory focus in 2018, including cybersecurity risk, asset management products and activities, resolution, central counterparties, money market funds,

financial data quality and sharing and financial technology. We intend to deal with the most interesting of these in separate blog posts by topic area.

[1] On November 17, 2017, in response to the [Presidential Memorandum](#) of April 2017, the Treasury Department released a report on its review of the FSOC's SIFI and SIFMU determination and designation processes under section 113 and section 804 of the Dodd-Frank Act ("[Treasury FSOC Report](#)"). Before the Treasury FSOC Report, the Treasury Department provided its view on the FSOC's role partially in its report on banks and credit unions ("[Treasury Bank and Credit Union Report](#)") in June 2017 and its report on asset management and insurance in October 2017 ("[Treasury Asset Management and Insurance Report](#)").

[2] [2017 Annual Report](#) at 4.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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